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No. 04 472

In The
# Supreme Court of the United States

H&R BLOCK, INC.; H&R BLOCK GROUP, INC.; H&R BLOCK SERVICES, INC.; H&R BLOCK TAX SERVICES, INC.; H&R BLOCK EASTERN TAX SERVICES, INC.; H&R BLOCK EASTERN TAX COMPANY, LLC; H&R BLOCK EASTERN ENTERPRISES, INC.; H&R BLOCK EASTERN SUPPORT SERVICES, LLC,

*Petitioners,*

v.

ERIN M. McNULTY and BRIAN J. ERZAR, on behalf of themselves and all others similarly situated,

*Respondents.*

**On Petition For A Writ Of Certiorari To The Superior Court Of Pennsylvania**

## PETITION FOR A WRIT OF CERTIORARI

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## QUESTIONS PRESENTED

1. Whether, when an arbitration clause in a contract specifies that the issue of the arbitrability of a dispute is to be decided by the arbitrator, a court still retains the power to decide that a particular dispute falls outside the scope of the agreement to arbitrate?

2. Whether, when an arbitration clause in a contract specifies that the validity and enforceability of the clause is to be decided by the arbitrator, a court still retains the power to decide that the agreement to arbitrate is unconscionable as applied to a particular dispute because it calls for the plaintiff to pay a small fee that could exceed the amount of money at stake in the dispute?

3. Whether the possibility that a plaintiff might be assessed an arbitration fee exceeding the small amount of money at stake provides a valid legal basis for excusing a plaintiff from abiding by an otherwise valid arbitration agreement.

## CORPORATE DISCLOSURE STATEMENT

Petitioner H&R Block, Inc., is a publicly held company traded on the New York Stock Exchange. Each of the other petitioners is a direct or indirect subsidiary of H&R Block, Inc. No publicly held company owns 10% or more of the stock of H&R Block, Inc., and no publicly held company other than H&R Block, Inc. owns 10% or more of any of the other petitioners.

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Petitioners H&R Block, Inc., *et al.*, respectfully request that the Court grant a writ of certiorari to review the judgment of the Superior Court of Pennsylvania.

## OPINIONS BELOW

The opinion of the Superior Court of Pennsylvania is reported at 843 A.2d 1267 and is reproduced in Appendix A, at A-1. The order of the Supreme Court of Pennsylvania denying Petitioners' Petition for Allowance of Appeal is set forth in Appendix B, at A-15. The relevant portion of the unreported opinion of the Court of Common Pleas of Lackawanna County, Pennsylvania, is reprinted in Appendix C, at A-16.

## JURISDICTION

The opinion and judgment of the Superior Court of Pennsylvania were filed on February 26, 2004. Petitioners' timely Petition for Allowance of Appeal was denied by the Pennsylvania Supreme Court on July 1, 2004. This petition was filed within 90 days of July 1, 2004. The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(a) An interlocutory ruling of a state court refusing to enforce an arbitration clause, once appealed as far as possible within the state court system, is "final" for purposes of section 1257(a). *Southland Corp. v. Keating*, 465 U.S. 1, 6-7 (1984).

## STATUTE INVOLVED

Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, provides:

> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part

> thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

## STATEMENT

Petitioners H&R Block, Inc. and several of its affiliate companies (collectively "Block") seek review of ruling by the Pennsylvania Superior Court refusing to enforce an arbitration agreement. Displaying a remarkable degree of hostility to arbitration agreements despite the contrary mandate of the Federal Arbitration Act ("FAA"), the court chose to decide for itself that the underlying dispute did not fall within the scope of the arbitration clause invoked by petitioners. It did so even though the clause *expressly* states that questions of arbitrability are to be decided in arbitration. And it did so based not on the language of the arbitration clause but on suppositions derived from the "surrounding circumstances" and "the objects [the parties] apparently had in view." Pet. App. A-9. The court then went on to hold, in the alternative, that a $50 fee plaintiffs might have to pay to the arbitrator rendered the arbitration clause *per se* unconscionable and unenforceable.

Petitioners ask the Court to grant review to consider whether, consistent with the FAA, the court acted properly in addressing either the scope or the enforceability of the arbitration clause and whether federal law allows a party to evade an arbitration agreement in a form contract based on the possibility of a fee matching or exceeding the small amount of relief at stake. As we show, there is a clear need for clarification of the law with respect to all of these questions.

*Factual Background*

Block is a provider of income tax preparation services to individual taxpayers. Both respondents retained Block for that purpose. During the course of the tax preparation process, they made the choice to have Block file their returns electronically, for a fee ranging from $34 to $37. Because they were filing electronically, they became eligible to be offered Refund Anticipation Loans ("RALs") from Household Bank, F.S.B. A RAL is a short-term loan secured by, and payable from, the tax refund respondents expected to receive from the IRS.

Respondent McNulty applied for RALs in 2000 and 2002; respondent Erzar did the same in 1999 and 2001. Both submitted RAL applications from the Block office where their tax returns were prepared. The RAL application forms executed by respondents each contained a section similar in all material respects to the following excerpt from Brian Erzar's 2001 RAL application,[1] in which the parties agree that

> any claim, dispute or controversy, whether in contract [or] tort (intentional or otherwise), whether pre-existing, present or future, and including constitutional, statutory, common law, regulatory, and equitable claims with HB . . . in any way relating to [the loan documents] . . . and/or (c) the relationships of the parties, including the validity, enforceability or scope of this Arbitration Provision or any part

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[1] Although the Arbitration Provision contained in each of their applications varied slightly from year to year, the differences were not considered material by the Superior Court, Pet. App. A-5, and are immaterial for purposes of the Questions Presented. The 2001 form as signed by respondent Erzar is set out in its entirety in Appendix D, at A-32.

> thereof . . . shall be resolved, upon the election of either [party], by binding arbitration pursuant to this Arbitration Provision. . . .

Pet. App. A-32.[2]

The same section of the agreement went on to provide that "the term 'HB' shall mean Household Bank, f.s.b., and H&R Block, Inc., and each of their parents, wholly or majority-owned subsidiaries, affiliates, [and other related entities]." Pet. App. A-35. Thus, although Block was not technically a party to the loan transaction that it offered its tax preparation customers, those customers who decided to take a RAL expressly agreed to arbitrate all disputes with Block relating to the loan *or* relating to their "relationship" with Block. They further agreed that disagreements about the scope of the arbitration agreement would be addressed in the first instance by the arbitrator.

The arbitration section of the agreement further provided that the plaintiff in a dispute would pay the first $50 of the filing fee owed to the arbitrator, that Block would pay the remainder of the filing fee and any administrative or hearing fees up to at least $1500, that a prevailing plaintiff could receive a reimbursement of any fees paid from Block, and that Block, if it prevailed, would not recover fees it had paid from the plaintiff. Pet. App. A-32 - 33.

*Proceedings Below*

Respondents filed this lawsuit in the Court of Common Pleas of Lackawanna County, Pennsylvania, in August 2002.

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[2] The customer also expressly waived any right to participate in any class action against Block. Pet. App. A-34. The arbitration agreement also recited that it was "made pursuant to a transaction involving interstate commerce, and shall be governed by the Federal Arbitration Act, 9 U.S.C. Sections 1-16." Pet. App. A-33.

In their First Amended Class Action Complaint filed in November 2002, they sought to represent a class of all Pennsylvania customers of Block who had paid an electronic filing fee to Block since August 31, 1996. They alleged that Block had improperly charged them $34 or $37 for filing their tax returns electronically and had deceptively portrayed electronic filing as a necessary component of Block's tax preparation services. They asserted claims against Block for breach of fiduciary duty, breach of contract, breach of the duty of good faith and fair dealing, unjust enrichment, and violation of the Pennsylvania Unfair Trade Practices and Consumer Protection Law. Each claim is premised on the contention that Block should have explained to respondents that they could have instead mailed their tax returns to the IRS or possibly have filed the returns electronically for free or at a discounted fee, or telephonically for free through a program not available to all customers.

Block filed Preliminary Objections, which included a motion to compel arbitration pursuant to the FAA. Block argued that respondents' claims regarding the electronic filing fee fell within the scope of respondents' "relationship" with Block, as referenced in the Arbitration Provision of the RAL application. Respondents resisted arbitration on the ground that the Arbitration Provision, though valid, was not applicable to their claims because the transaction in which Block charged the electronic filing fee was "separate and distinct" from the RAL transaction. Pet. App. A-26.

The trial court refused to order arbitration. It first rejected Block's contention that respondents' objections to the scope of the arbitration provision — *i.e.*, the issue of arbitrability — should be resolved by the arbitrator. Pet. App. A-22 - 23. It then agreed with respondents' argument "that the electronic filing practices are separate and distinct from the RAL" and that electronic filing can be done independently of the RAL. Pet. App. A-26. It also ruled that

the "mere mention of Block in the RAL documents, without more, does not mean [that the Arbitration Provision] applies to the narrow claim" made by respondents. Pet. App. A-26. Block's motion to compel arbitration was thus denied. The court refused to address respondents' additional theory that the arbitration provision was unconscionable, saying that would be a matter for the arbitrator to decide if the arbitration provision were applicable to this dispute. Pet. App. A-27.

Block appealed to the Superior Court of Pennsylvania, which affirmed the trial court's ruling. The three-judge panel first addressed the question whether the trial court acted properly in even addressing the dispute over the applicability of the arbitration clause in the RAL agreement to a claim relating to Block's electronic filing fee. It saw no error there, even though the arbitration clause specifically states that any disputes over the scope of the agreement are themselves subject to mandatory arbitration. The court reasoned that requiring a plaintiff to proceed to arbitration whenever Block asserted the defense of the arbitration clause -- at least for purposes of determining whether the claim at issue is within the scope of the arbitration agreement -- "would produce absurd and inequitable results." Pet. App. A-7. In so doing, the court imagined a case where a customer fell and incurred an injury on Block's premises and Block claimed that the arbitration clause covered the resulting personal injury lawsuit. Pet. App. A-7 - 8. The court then simply cited Pennsylvania case law holding that the arbitrability of a dispute "is a matter of law for a court [to] decide," Pet. App. A-8, -- a principle that is well recognized *except* where the arbitration agreement specifies otherwise.

The Superior Court then affirmed the trial court's ruling that the electronic filing fee claim at issue fell outside the scope of the arbitration clause. The court acknowledged that the clause contained "expansive language," Pet. App. A-7, and never disputed that the filing fee claim fell within its

literal terms -- since it involved a "claim, dispute or controversy . . . with [Block] . . . in any way relating to . . . the relationships of the parties." Pet. App. A-5 (quoting loan document). But the court concluded that the arbitration clause extended only to "the relationships of the parties as it applies to the loan." Pet. App. A-10 In so doing, it relied on an analysis of "the surrounding circumstances, the situation of the parties when the contract was made, and the objects they apparently had in view and the nature of the subject matter." Pet. App. A-9. This holding effectively rendered the "relationships" language in the arbitration clause superfluous, since the clause separately covered disputes in any way relating to the loan documents. *See* Pet. App. A-32.

As an alternative basis for affirmance, the appellate court also ruled that the Arbitration Provision was unconscionable because it required the claimant to pay a $50 filing fee. Pet. App. A-12 - 14. Here again, the court gave no apparent weight to the fact that the arbitration agreement explicitly states that disputes about the "validity, scope and enforceability of this Arbitration Provision . . . shall be resolved . . . by binding arbitration." It simply assumed the power to address the unconscionability issue.

In so doing, the court noted that Block must pay the next $1,500 of any costs above the initial $50 fee. While it also suggested that a plaintiff might end up paying fees above $1550, the court explicitly did not rely on that possibility. Instead, it flatly held that the requirement of a $50 fee payment is unconscionable as applied to a dispute where the amount a plaintiff might hope to recover is in the range of $30. Pet. App. A-13. In reaching this conclusion, the court gave no weight to the fact that the arbitration agreement provides that prevailing plaintiffs may recover any fees they have paid from the losing defendant (whereas a prevailing defendant has no such right). Nor did it take into account the possibility that the arbitrator might waive the fee in a given

case or might hold the fee requirement itself to be unconscionable.

Block timely petitioned for discretionary review ("allocatur") to the Pennsylvania Supreme Court. That petition was denied on July 1, 2004. Pet. App. A-15.

## REASONS FOR GRANTING THE PETITION

This case raises several important and recurring issues relating to the duty of all state and federal courts under the FAA to respect and enforce agreements to arbitrate future disputes. In particular, the Court has repeatedly held that while the "arbitrability" of a particular dispute is generally a matter for a court to decide, the parties to a contract are free to agree that this initial question will itself be resolved in arbitration. *See First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 943 (1995); *AT&T Technologies, Inc. v. Communications Workers of Am.*, 475 U.S. 643, 649 (1986). As this case illustrates, however, there remain at least two uncertainties about the impact of such an agreement to "arbitrate arbitrability" that the Pennsylvania court exploited in its zeal to find a way to avoid sending respondents' claims to arbitration. The result was that petitioners, having legitimately sought to do business only with customers who agreed to arbitrate all aspects of any future legal dispute, now find themselves facing a statewide class action.

The first uncertainty the Court needs to address involves the question whether, when the parties have clearly and unmistakably agreed to allow the arbitrator to resolve fights about the "scope" of their agreement to arbitrate, the courts nevertheless retain authority say that a given dispute is so clearly outside the scope of the arbitration agreement that the arbitrability issue need not be resolved in arbitration. Although the Superior Court in this case claimed such authority, nothing in the FAA or this Court's precedents

supports that claim. Nor is there any practical reason to recognize such a limitation on the power of contractual parties to allocate authority between the courts and arbitrators. To the contrary, under the FAA, courts trust arbitrators to apply the law fairly -- including in cases when their own authority over a dispute is being debated by the parties. And the dangers of allowing courts to short-circuit that process where it thinks a particular dispute plainly is not arbitrable are well illustrated by this case: if this loophole exists, courts will use it even where, as here, the language of the arbitration clause is broad enough to cover the dispute at issue and a contrary conclusion requires dubious assumptions about the parties' goals and unstated intent at the time of contract formation.

The second uncertainty arises from the fact that the parties here agreed to arbitrate not only disputes about the scope of the arbitration clause but also disputes about its "validity" and "enforceability." Such language would seem to require that an attack on the arbitration agreement as unconscionable be addressed in the first instance in arbitration. But the Pennsylvania court did not even pause to consider that question as it proceeded to hold that because the arbitration provision calls on petitioner to pay a $50 fee to the arbitrator, it cannot be enforced when the dispute involves a smaller sum like $30. The Court thus needs to make clear that the parties' power to allocate authority between the courts and the arbitrator extends to the kind of unconscionability arguments that are raised nearly every time a defendant demands that a lawsuit be stayed or dismissed based on a prior arbitration agreement.

Indeed, in the wake of several recent decisions of this Court including *PacifiCare Health Systems, Inc. v. Book*, 538 U.S. 401 (2003), and *Green Tree Financial Corp. v. Randolph*, 531 U.S. 79 (2000), there is much to be said in favor of a rule that these kinds of as-applied fairness attacks

on an arbitration agreement should always be addressed first in arbitration, even where there has been no agreement to send disputes about the validity and enforceability of the agreement to arbitration. In essence, the rule would be that although courts generally address the *scope* of an arbitration agreement (absent an agreement to arbitrate arbitrability like the one here), if a particular dispute falls within that scope, other arguments about enforceability based on the prospect of paying high fees or receiving unduly limited relief in arbitration should go to the arbitrator. In *PacifiCare* and *Green Tree*, the Court has held that arbitration cannot be evaded based on speculative concerns about available remedies or costs. But the reality is that those concerns will almost always be somewhat speculative *ab initio*, and where the parties have agreed to arbitrate a particular type of dispute, there is no persuasive reason why these other concerns should not go first to the decisionmaker they jointly selected.

Finally, turning to the substance of the Superior Court's unconscionability holding, there is yet another unresolved question -- whether the prospect of agreed arbitration fees exceeding the amount of money at stake can ever provide a basis for allowing plaintiffs to litigate their claims in court. If courts are going to be addressing arguments up front that enforcing an arbitration agreement would be unconscionable or violate public policy, there need to be appropriate limits established that are consistent with the policies of the FAA. For example, the Court might well decide that parties should be free to limit themselves to fora and procedures that will make it impracticable to litigate small claims. Alternatively, it might say that when fees exceed potential recovery, the arbitration may proceed but the arbitrator is dutybound to consider whether the fees are unconscionable as applied to a given dispute. Given the high number of cases in which these kinds of arguments against arbitration are being raised,

and the widely disparate rulings produced in response, there are compelling reasons for this Court to provide guidance about how courts should proceed.

## I. THE COURT SHOULD MAKE CLEAR THAT WHEN PARTIES HAVE AGREED TO HAVE THE ARBITRABILITY OF PARTICULAR DISPUTES DECIDED IN ARBITRATION, COURTS RETAIN NO AUTHORITY TO REFUSE TO SEND A GIVEN DISPUTE TO ARBITRATION FOR THAT PURPOSE.

This Court in *AT&T Technologies, Inc.* acknowledged the general rule that "the issue of arbitrability is for the courts to decide unless the parties stipulate otherwise," but held that if the parties "clearly and unmistakably" say so, the arbitrator is to decide arbitrability. This rule was reaffirmed in *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 943 (1995), where the Court said that "the question 'who has the primary power to decide arbitrability' turns upon what the parties agreed about *that* matter. Did the parties agree to submit the arbitrability question itself to arbitration?" *See also Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79, 83 (2002) (recognizing the same rule).

In the present case, the answer to the question posed in *First Options* is plainly "yes." The parties "clearly and unmistakably" agreed that the "scope" of the arbitration provision would be decided by the arbitrator. The contract provides that disputes over various matters including "including the validity, enforceability or scope of this Arbitration Provision or any part thereof" should be resolved in arbitration. But the court below arrogated to itself that determination by holding that the dispute over the electronic filing fee was not within the scope of the arbitration clause.

In so doing, it departed from the rulings of various federal appellate courts, interpreting similar language, which

have held that arbitrators should address arbitrability when the parties so agreed. *See e.g., Shaw Group, Inc. v. Triplefine Int'l Corp.*, 322 F.3d 115, 121-22 (2d Cir. 2003) (agreement referring "[a]ll disputes . . . concerning or arising out of" the agreement to arbitration included issue of arbitrability); *Air Line Pilots Ass'n v. Midwest Express Airlines, Inc.*, 279 F.3d 553, 556 (7th Cir. 2002) ("[W]hen an arbitration clause is so broadly worded that it encompasses disputes over the scope or validity of the contract in which it is embedded, issues of the contract's scope or validity are for the arbitrators."); *Southern California Dist. Council of Laborers v. Berry Constr., Inc.*, 984 F.2d 340, 344 (9th Cir. 1993) (arbitration clause covering questions over "interpretation or application of the terms" of labor agreement left arbitrability determination to arbitrator).

The Pennsylvania court, however, was not willing to follow the clear dictates of the contract and this Court's decisions. This was particularly remarkable given the nature of the arbitration clause at issue. As the Seventh Circuit said when it addressed the same contractual language:

> It would be hard to draft a broader clause. This covers all claims 'relating to' the 1999 loan plus all disputes 'relating to' any earlier tax year and any preceding refund-anticipation loan. It also covers any dispute about 'the validity or enforceability of this arbitration provision or any part thereof' — a clause evidently tailored to come within the rule that people may agree to arbitrate whether a dispute is arbitrable. *See First Options* . . . .

*Carbajal v. H&R Block Tax Services, Inc.*, 372 F.3d 903, 905 (7th Cir. 2004).

To be sure, there may be some temptation to say that when a given dispute falls clearly outside the scope of a prior agreement to arbitrate, a court should be able to so conclude and proceed with adjudicating the case, rather than having to

ask an arbitrator to confirm the obvious. But such a rule is fraught with danger, as this case shows. The danger is that courts eager to entertain claims and redress perceived injustice will be inclined to impose a narrow reading of the scope of the arbitration clause even where that reading is debatable. That was certainly what occurred here, where the contractual language provided no support for a narrow reading; in fact it stated that all disputes relating to the "relationships" of the parties were to be arbitrated. But the court below added its own narrowing gloss based on its assessment of the "surrounding circumstances" and "the objects [the parties] apparently had in view." Pet. App. A-9. The Court should give careful consideration to whether allowing courts to short-circuit the decisionmaking process that the parties specified will all too often lead to this kind of abuse.[3]

In that regard, it is important to recognize the effects that even a few "outlier" rulings refusing to enforce an arbitration agreement can have on a company dealing with a large number of customers. Block, for example, has 9,851 offices in the United States, with operations in every state. During the most recent tax year, it prepared almost 16,000,000 tax returns, including about 15.6% of all individual federal tax returns filed. During that same period, more than 4,200,000 RALs were processed, with each applicant signing the arbitration agreement at issue in this case. Similar numbers

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[3] Nor is this necessarily an isolated case. In *Weitz Co v. Shoreline Care Ltd. Partnership*, 666 A.2d 835 (Conn. Ct. App. 1995), for example, the appellate court upheld the decision of a trial court enjoining an arbitrator from proceeding, after the arbitrator had already decided that he had the power to decide arbitrability. The court held that the contract language was "clear and unambiguous" that the arbitration clause did not apply to the dispute, essentially justifying removal of the dispute from the arbitrator based on the obvious language of the statute. *Id.* at 837.

exist for earlier years.[4] This even-handed Arbitration Provision has been developed over the years to provide an efficient, less expensive method of dispute resolution that will adjudicate controversies between the parties without judicial involvement.

Courts generally have heeded this Court's FAA rulings and have allowed the parties' clearly expressed intent to be implemented through arbitration. But as in this case, a single contrary ruling by one state or federal court can lead to certification of a statewide or even nationwide class numbering in the thousands or millions, even where every one of those class members agreed to arbitrate disputes individually *and* agreed to arbitrate disagreements over the scope of the arbitration provision.

The Pennsylvania opinion will also be seized on by class-action lawyers in other states as precedent for avoiding this Court's rulings and eviscerating the Arbitration Provision at issue here. The importance and increasing use of arbitration as a judicial stress-reliever, the conflicts between the decision below and both Block and non-Block decisions elsewhere, and the disturbing disdain for this Court's jurisprudence evidenced in this case all confirm the need for review here. Indeed, the issue is so important, the error below so plain, and its potential effects so widespread, that summary reversal would be appropriate. *See Citizens Bank v. Alafabco, Inc.* 539 U.S. 52 (2003) (refusal of state court to apply FAA to require arbitration of dispute over loan transaction summarily reversed).

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[4] The information is contained in Block's annual report, available at http://www.corporate-ir.net/ireye/ir_site.zhtml?ticker=HRB&script=700.

## II. THE PENNSYLVANIA SUPERIOR COURT ERRONEOUSLY USURPED THE ROLE OF THE ARBITRATOR BY PREMATURELY CONCLUDING THAT THE REQUIREMENT THAT THE CLAIMANT PAY A $50 FILING FEE RENDERED THE ARBITRATION AGREEMENT UNCONSCIONABLE

Any lingering doubt about the extent of the hostility to arbitration that existed below was laid to rest by the Superior Court's alternative — and gratuitous — holding that the provision in the Block arbitration clause requiring the claimant to pay a $50 filing fee is "unconscionable" and renders the entire Arbitration Provision unenforceable. Pet. App. A-12 - 13. This ruling likewise presents important issues of federal law and conflicts with numerous other decisions. The problems with the Pennsylvania court's pronouncement are manifold and profound:

1. The arbitration provision at issue plainly states that disputes over the "validity" and "enforceability" of the arbitration agreement should go to arbitration. Yet the Superior Court saw no reason to avoid proceeding to address the unconscionability issue itself. In so doing, it contradicted the express dictates of the contracting parties.

This Court has not had an opportunity to address the question whether the power of the parties to determine in advance which issues will be decided judicially and which will go to arbitration extends to questions of enforceability relating to claims of unconscionability. But there is every reason to think that the power to agree to "arbitrate arbitrability" should include a related power to agree to arbitrate validity and enforceability. *See Berkley v. H & R Block Eastern Tax Servs., Inc.*, 30 S.W.3d 341 (Tenn. Ct. App. 2000) (analyzing nearly identical arbitration clause language and holding that arbitrator must decide questions of

validity and enforceability of arbitration clause). The Court should grant review here to make that clear.

Indeed, far from supporting the notion that enforceability determinations are reserved for the courts in all cases, this Court's recent rulings have moved in the opposite direction. The Court has shown increasing skepticism about efforts to avoid arbitration of disputes that are concededly within the substantive scope of an arbitration agreement, based on claims about excessive costs, unduly limited relief, and the like.

First, in *Vimar Seguros y Reaseguros, S.A. v. M/V Sky Reefer*, 515 U.S. 528 (1995), the Court rejected efforts to avoid referral of a dispute to a Japanese arbitrator based on speculative concerns that the arbitrator might not apply American law and thus might reduce the recovery that federal law deemed appropriate. Five years later, in *Green Tree Financial*, a case involving a claim under the federal Truth in Lending Act, the Court rejected the argument that a court could withhold enforcement of an arbitration clause based on the risk that the plaintiff would be "required to bear prohibitive arbitration costs if she pursue[d] her claims in an arbitral forum, and thereby force[d] to forgo any claims she may have[.]" 531 U.S. at 90. The Court stated that to bar arbitration on this basis, the plaintiff would have to make a clear showing that such an outcome is very likely. *Id.* at 91-92.

Two years ago, the Court in *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79 (2002), addressed the question of who should apply a rule of the National Association of Securities Dealers requiring that claims eligible for arbitration be submitted within six years. After the plaintiff invoked arbitration, the defendant filed suit asking for an order barring the arbitration. It argued that the time limit was a matter of "arbitrability" and thus within the courts'

jurisdiction. This Court rejected that argument, drawing a distinction between the question whether a given dispute falls within the scope of an arbitration agreement (which courts generally decide) and other procedural issues like timeliness and waiver that go to the arbitrator. *Id.* at 84-85.

Then, in *PacifiCare Health Systems*, the Court dealt with an argument that the relief available in arbitration, which by agreement excluded "punitive damages," precluded sending civil RICO claims to arbitration because the RICO statute authorizes awards of treble damages. Concluding that the meaning of the arbitration agreement was ambiguous as applied to RICO treble damages, the Court held that the all questions about the meaning of the agreement and the enforceability of the limitation on damages in the agreement should go first to the arbitrator for resolution. 538 U.S. at 406-07.

This line of cases strongly suggests that while questions about the scope of the arbitration agreement are presumptively within the courts' bailiwick, questions of enforceability based on the prospect of high arbitration costs should presumptively be sent to the arbitrator -- even in the absence of an explicit agreement to arbitrate enforceability like the one present here. A number of courts of appeals have adopted that view. For example, in *Bob Schultz Motors, Inc. v. Kawasaki Motors Corp., U.S.A.*, 334 F.3d 721, 726-27 (8th Cir. 2003), *cert. denied*, 124 S. Ct. 1147 (2004), the Eighth Circuit held that an unconscionability challenge to an arbitration provision providing that the "loser pays" all costs and expenses "was properly presented to the arbitrator and not the District Court." The Eleventh and First Circuits have agreed. *See Musnick v. King Motor Co. of Ft. Lauderdale*, 325 F.3d 1255, 1258-62 (11th Cir. 2003) (ordering arbitration in a Title VII case despite presence of a "loser pays" provision because it was speculative whether plaintiff would be assessed fees and challenge to the validity of such a

procedure is more properly raised in court after arbitration); *Thompson v. Irwin Home Equity Corp.*, 300 F.3d 88, 92 (1st Cir. 2002) (same); *see also Carbajal*, 372 F.3d at 906 (rejecting party's effort to evade arbitration of federal statutory claim based on absence of potential for statutory fee award because "the arbitrator rather than the court determines the validity of these ancillary provisions") (citing *PacifiCare*); *Great Western Mortgage Corp. v. Peacock*, 110 F.3d 222, 232 (3d Cir. 1997) (argument against arbitration premised on plaintiff's prospective inability to collect statutory punitive damages "is separate and apart from the issue of whether an employee has agreed to an arbitral forum, and hence, is for the arbitrator to decide"); *Larry's United Super, Inc. v. Werries*, 253 F.3d 1083, 1086 (8th Cir. 2001) ("At this juncture, our jurisdiction extends only to determine whether a valid agreement to arbitrate exists, not to determine whether public policy conflicts with the remedies provided in the arbitration clause.").

By contrast, in a number of other cases, courts have addressed enforceability arguments based on unconscionability or public policy themselves. The Ninth Circuit, for instance, has adopted a *per se* rule that arbitrator fee-splitting provisions in employment contracts render an arbitration agreement unenforceable. *See Circuit City Stores, Inc. v. Adams*, 279 F.3d 889, 894 & n.5 (9th Cir. 2002); *see also Ingle v. Circuit City Stores, Inc.*, 328 F.3d 1165, 1178-79 (9th Cir. 2003) (holding same and that remedy limitation provisions made arbitration agreement substantively unconscionable), *cert. denied*, 124 S. Ct. 1169 (2004); *Banc One Acceptance Corp. v. Hill*, 367 F.3d 426, 429-31 (5th Cir. 2004) (addressing unconscionability); *Iberia Credit Bureau, Inc. v. Cingular Wireless LLC*, 379 F.3d 159, 165 n.6 (5th Cir. 2004) (same); *Investment Partners, L.P. v. Glamour Shots Licensing, Inc.*, 298 F.3d 314, 316 (5th Cir. 2002) (addressing limitation of remedies).

As noted *infra*, arbitration cost concerns are almost always speculative and there is no reason why an arbitrator cannot fairly address their propriety in the first instance. Nor is there any reason to draw a distinction between arguments about prospective costs based on public policy and the statutes being enforced -- as in *Musnick*, and *Thompson* -- and arguments based on state-law principles of unconscionability. *See Bob Schultz Motors*, 334 F.3d at 726-27 (applying *Thompson* and holding that question of unconscionability must go to arbitrator).

In either setting, once courts defer, the arbitrator is then free to determine whether the cost provisions in the arbitration agreement should be enforced or disregarded, while the agreement to arbitrate remains in place. *See Musnick*, 325 F.3d at 1261 n.7 (although contract specifies that loser "shall" pay costs and fees to the prevailing party, "at least three circuits have held that the arbitrator may determine whether contractual limitations on remedies are enforceable"). Here, by contrast, the court used the *possibility* of what it saw as an excessive fee as a basis for abrogating the arbitration agreement altogether. That hardly makes sense. Clearly, a decision from this Court addressing who should entertain these kinds of challenges to arbitration clauses would be extremely helpful to the lower courts.

2. Even assuming that the court below acted appropriately in addressing the merits of the unconscionability argument itself, the final question presented here is whether it acted correctly and consistently with the dictates of the FAA when it refused to enforce the arbitration agreement on that basis. There are several reasons to conclude that it did not.

First, the Court gave no weight to the fact that respondents might not have to pay the $50 fee. That was true for several reasons. To begin with, the balance of the costs

provision, which the court simply ignored, (a) requires Block to pay the balance of the fees charged by the arbitration administrator up to $1,500, (b) allows claimants to recover fees paid if they prevail, and (c) does not require them to reimburse Block for arbitration fees if Block wins. Pet App. A-32 - 33. Because of these provisions, it was erroneous for the court to decide this question based on a simple comparison of the potential fee -- $50 -- and the potential recovery -- around $30. If respondents were to recover the $30 in damages, they would also have had the $50 fee reimbursed.

Moreover, leaving that possibility aside, there was a second possibility: the arbitrator might simply have waived the fee, either discretionarily or based on a determination that it would be unconscionable in this particular case. Most arbitration regimes provide for waiver of fees in the case of hardship. *See e.g., Smith v. EquiFirst Corp.*, 117 F. Supp. 2d 557, 564 (S.D. Miss. 2000) (potentially high arbitration fees do not invalidate arbitration provision where National Arbitration Forum allows waiver of fees); *Herrington v. Union Planters Bank*, 113 F. Supp. 2d 1026, 1034 (S.D. Miss. 2000) (costs of arbitrator not a factor since American Arbitration Association "provides a procedure to waive fees"), *aff'd*, 265 F.3d 1059 (5th Cir. 2001) (unpublished table decision). The potential availability of such a waiver further illustrates the uncertainty of the cost picture at this juncture. For these reasons, respondents did not even approach the kind of non-speculative showing of prohibitive costs demanded in *Green Tree Financial*.

But the ruling below also raises a more fundamental issue. Even assuming that the $50 fee was a certainty and thus would preclude arbitration of a claim to $30, the question would remain whether, consistent with the FAA, a court may apply state-law unconscionability principles to invalidate an arbitration agreement just because that

agreement will effectively preclude litigation of very small claims. The same argument, after all, could be made with respect to any arbitration agreement that precludes class actions, regardless of whether up-front fees are imposed on the plaintiffs. Even without such fees, the arbitration agreement would effectively preclude litigation of claims (like the one present here) that are so small they will never be litigated or arbitrated individually.

In recent years, numerous courts have been confronted with this more fundamental question whether an arbitration provision that prevents classwide litigation of very small claims is unconscionable or enforceable. They have reached highly divergent results. *Compare Szetela v. Discovery Bank*, 97 Cal. App. 4th 1094, 1101 (Cal. Ct. App. 2002), *cert. denied*, 537 U.S. 1226 (2003), and *State ex rel. Dunlap v. Berger*, 567 S.E.2d 265, 280 (W. Va. 2002) (both holding arbitration provisions prohibiting class actions are unconscionable)[5] *with Ranieri v. Bell Atlantic Mobile*, 304 A.D.2d 353 (N.Y. App. Div. 2003) *and AutoNation USA Corp. v. LeRoy*, 105 S.W.3d 190, 200 (Tex. App. - Houston [14th Dist.] 2003, no writ) (prohibition on class actions not unconscionable).[6] The reasoning behind the Pennsylvania

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[5] For other decisions holding that prohibitions on class actions in arbitration agreements are unconscionable, *see, e.g. Ingle*, 328 F.3d at 1176; *Luna v. Household Fin. Corp.*, 236 F. Supp. 2d 1166, 1179 (W.D. Wash. 2002); *Lozada v. Dale Baker Oldsmobile, Inc.*, 91 F. Supp. 2d 1087, 1105 (W.D. Mich. 2000); *BellSouth Mobility LLC v. Christopher*, 819 So. 2d 171, 173 (Fla. Ct. App. 2002); *Leonard v. Terminix Int'l Co.*, 854 So. 2d 529, 539 (Ala. 2002).

[6] For other decisions holding that prohibitions on class actions are not unconscionable, *see, e.g., Snowden v. CheckPoint Check Cashing*, 290 F.3d 631, 638-39 (4th Cir. 2002), *cert. denied*, 537 U.S. 1226 (2003); *Vigil v. Sears National Bank*, 205 F. Supp. 2d 566, 573 (E.D. La. 2002); *In re Real Networks, Inc. Privacy Litig*, No. 00-C-1366, 2000 WL 631341, at *7 (N.D. Ill. May 8, 2002); *Gras v. Associates First Capital*

court's opinion - that small claims must be litigated even if the parties are deprived of the agreed-upon contractual choice of forum - is the same that has led courts to strike down arbitration provisions that prevent maintaining claims as class actions. *See, e.g., Szetela*, 97 Cal. App. 4th at 1101 (contractual prohibition of class actions is "harsh and unfair" to customers with small claims); *Dunlap*, 567 S.E.2d at 278.

But, the policies of the FAA would seem to dictate that a valid agreement to arbitrate should be respected and cannot be evaded every time a plaintiff asserts a claim worth less than the costs of arbitration. As the Seventh Circuit put it in *Carbajal*, addressing the same arbitration provision at issue here,

> Is enforcement of this clause unconscionable? How could it be? Arbitration is just a forum; people may choose freely which forum will resolve their dispute.

372 F.3d at 905-06.

Moreover, addressing the argument that the agreement was invalid because it required waiver of a right to recover fees and costs if a plaintiff prevailed, the *Carbajal* court added that "people are free to opt for bargain-basement adjudication" and that remains true even if the choice includes a waiver of rights, because "no general doctrine of federal law prevents people from waiving . . . rights . . . in exchange for other things they value more, such as lower prices or reduced disputation." *Id.* at 906-07. As the Seventh Circuit put it in a different case, arguments based on the costs of arbitration and preclusion of class actions are "the sort of litany that the federal Arbitration Act is supposed to silence." *Metro East Center for Conditioning & Health v. Qwest*

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*Corp.*, 786 A.2d 886, 888-93 (N.J. Super. Ct. App. Div. 2001); *Edelist v. MBNA America Bank*, 790 A.2d 1249, 1261 (Del. Super. Ct. 2001).

*Communications Int'l, Inc.*, 294 F.3d 924, 927 (7th Cir. 2002).

The court below, by contrast, effectively created a *per se* rule that an arbitration agreement becomes unenforceable whenever the value of the claim at issue is so small that the court thinks a class action is the only way to get it adjudicated. Because such a rule would gut the FAA in cases involving small but widespread claims, the ruling below on this issue merits review as well.

## CONCLUSION

The writ of certiorari should be granted.

Respectfully submitted,

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## APPENDIX A

| | | |
|---|---|---|
| ERIN M. McNULTY AND BRIAN J. ERZAR, on behalf of themselves and all others similarly situated, Appellees | : | IN THE SUPERIOR COURT OF PENNSYLVANIA |
| v. | : | |
| H&R BLOCK, INC.; H&R BLOCK GROUP, INC.; H&R BLOCK SERVICES, INC.; H&R BLOCK TAX SERVICES, INC.; H&R BLOCK EASTERN TAX SERVICES, INC.; H&R BLOCK EASTERN TAX COMPANY, LLC; H&R BLOCK EASTERN ENTERPRISES, INC.; AND H&R BLOCK EASTERN SUPPORT SERVICES, LLC, Appellants | : | No. 679 MDA 2003 |

Appeal from the Order entered April 16, 2003
In the Court of Common Pleas of Lackawanna County,
Civil No. 02-CV-4654

BEFORE: KLEIN, BENDER and OLSZEWSKI, JJ.

OPINION BY KLEIN, J.: FILED: February 26, 2004

¶ 1 Plaintiffs, Erin McNulty and Brian Erzar, filed this class action lawsuit alleging that defendants ("Block") charged its clients millions of dollars in unnecessary fees for filing their tax returns electronically ("e-filing"). They further allege that Block deceptively said that the e-filing fee was a necessary and required component of standard

tax preparation, when in fact it cost Block next to nothing to file electronically, as compared to filing traditional paper returns.

¶ 2 Block filed preliminary objections to the complaint claiming that an arbitration provision in a separate contract with Household Bank requires these claims to be arbitrated individually and not tried in court as a class action.[1] The trial court determined that the arbitration provision did not cover the present claims because the e-filing fee was too removed from the loan application contract that contained the arbitration provision. After careful review of the parties' submissions, relevant case law, statutes, regulations and the record, we affirm, both on the rationale of the lower court and additional grounds.

¶ 3 In reviewing a ruling on preliminary objections, we must accept as true all well pled, material allegations in the complaint. ***DeFazio v. Gregory***, 2003 PA Super 418. Further, in determining the propriety of a denial of a preliminary objection in the nature of a petition to compel arbitration, we examine the trial court's ruling for abuse of discretion or error of law. ***Pittsburgh Logistics Systems, Inc. v. Professional Transportation and Logistics, Inc.***, 803 A.2d 776 (Pa. Super. 2002). Our scope of review is plenary. ***Huegel v. Mifflin Construction Company, Inc.***, 796 A.2d 350 (Pa. Super. 2002).

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[1] Block raised several other issues in preliminary objections as well. None of those issues are before us, as those rulings are interlocutory. Only the denial of transfer to arbitration is immediately appealable.

¶ 4 Block raises three issues on appeal:

> (1) The trial court improperly determined the claims presented are subject to judicial determination rather than allowing the arbitration panel to decide the issue;
>
> (2) the trial court erred in determining the claims did not involve the "relationship" between the parties, as described in the arbitration provision; and
>
> (3) the trial court erred in concluding the claims were not "intermeshed" with the application for the loan.

¶ 5 Because many of the facts necessary to resolve this appeal apply to multiple issues, we will address the issues as a whole. Before we address the merits, a review of the factual background is necessary.

**Background**

¶ 6 Block is a well-known, nationwide tax preparation service. One of the services offered by Block is known as "e-filing." The client's tax return is prepared on computer and is transmitted to the Internal Revenue Service electronically, rather than by the traditional paper return. In general, an electronic return is processed by the government faster than a paper return. A refund check, if the taxpayer is so entitled, is sent out in a shorter period of time. It is alleged by plaintiffs that Block charged McNulty a $37.00 fee to file electronically in both 2001 and 2002. Erzar was allegedly charged a $34.00 electronic filing fee in 2000.

¶ 7 Another option offered is a refund anticipation loan ("RAL").[2] This is a separate agreement (not with Block) from the actual filing of the tax return and there is no requirement that the client obtain an RAL. A taxpayer can obtain a loan, in this case from Household Bank, using the promise of a tax refund as security for the loan. While a refund processed through electronic filing will reach the taxpayer usually within two weeks, the RAL provides cash within one to four days. This service requires a separate contract with Household. The contract states that Block is the electronic return originator (ERO), typically as either tax preparer and/or filer. The contract also makes clear that Block has no other connection to the loan, specifically denying Block status as a fiduciary or agent.

¶ 8 Thus, Block is not an actual party to the loan – it provides no money to the client, is not responsible for the repayment of the RAL, nor does it process the loan. Block's connection to the loan process is that it may have filled out the tax form and it sent the form to the IRS.[3] The loan amount Household is willing to provide is presumably based upon the amount of the anticipated tax refund.

¶ 9 Although not a party to the contract itself, the contract also contains an arbitration clause that includes Block as a beneficiary to the clause. Household requires

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[2] An RAL is a short-term, high-interest loan that is secured by the anticipated tax refund. The RAL application form indicates that the estimated annual percentage rate based on loan amount and finance fee charged can be as high as 264%. The RAL fees are not at issue in this law suit.

[3] The RAL application, as noted, refers to Block as either the tax preparer **or** filer. Thus it appears that Block need not have actually prepared the tax return to apply for a loan.

that the RAL applicant file electronically with Block and, apparently for that reason, includes Block in the arbitration clause. In certain circumstances this makes a certain amount of sense as a complaint about the loan may include some allegation against Block. The arbitration clause has, at least partially, the purpose of guaranteeing all claims regarding the loan be heard together.

¶ 10 The arbitration clause contains very broad language regarding the scope and application of the clause. Specifically, the clause states:

> By signing this RAL application or the Loan Agreement (collectively the "Documents"), I hereby agree that any claim, dispute or controversy, whether in contract, tort (intentional or otherwise), whether pre-existing, present or future, and including constitutional, statutory, common law, regulatory and equitable claims with HB (as defined at the end of this paragraph) in any way relating to (a) the Documents or a similar documents [sic] for prior years . . . and/or (c) the relationships of the parties, including the validity, scope and enforceability of this Arbitration Provision . . . shall be resolved . . . by binding arbitration.

Loan application, para. 11.[4]

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[4] The various loan applications all contain similar language in the arbitration clause. No one disputes to this point. The arbitration clause appears in different paragraph numbers in the different applications. The language specifically cited herein is from Brian Erzar's RAL application.

**Issues**

¶ 11 The trial court determined that despite the broad language of the arbitration clause, that provision applied only to the loan transaction itself and not to any other service Block may have provided. The trial court concluded that the electronic fee charged for filing the tax form was a separate and distinct transaction from the application for a loan, and thus was not covered by the arbitration provision. The trial court pointed out that filing a tax return does not obligate one to obtain a loan; the administrative or processing charges incurred in filing a tax return will be incurred independent from any other transaction a customer may have with Household. Additionally, we note there is no indication at all in the record that Household in any way benefits from the e-filing fee or has any input as to the fee in any way.

¶ 12 In essence, the trial court found that charging a fee to push the "send" button (basically the equivalent of putting a stamp on an envelope) was too attenuated to the loan application process and so was exempt from the arbitration clause.

¶ 13 Block claims error in this determination for a number of reasons. First, it claims once the existence of an executed arbitration clause is established, that the arbitration clause clearly states that virtually any dispute regarding the arbitration provision must be arbitrated. There is certainly no doubt that plaintiffs executed RAL applications, all of which contain the arbitration provision. Thus, Block contends, all other considerations must be determined by a panel of arbitrators.

¶ 14 Block bases this argument at least partially on the Federal Arbitration Act (FAA), 9 U.S.C. §§ 1-16, which

governs arbitration provisions that involve interstate commerce. Specifically, the FAA states:

> [a] written provision in any maritime transaction or contract involving interstate commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract or transaction or refusal, shall be valid and irrevocable, and enforceable, save upon grounds as exist as law or in equity for the revocation of any contract.

9 U.S.C. § 2. The FAA represents a declaration of a liberal federal policy favoring arbitration, and so any doubts regarding the scope of arbitral issues should be resolved in favor of arbitration. ***Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.***, 460 U.S. 1, 24-25 (1983).

¶ 15 In essence, Block contends the combination of the expansive language of the arbitration provision – any disputes regarding the relationships of the parties, past, present or future is subject to arbitration – and the liberal policy favoring arbitration required the trial court to grant the transfer to arbitration once the existence of the provision was established. We believe that Block's interpretation is too broad.

¶ 16 First, as a matter of practicality, Block's interpretation would produce absurd and inequitable results. Imagine a situation where a customer goes to Block and has his taxes prepared. While on Block's premises as a business invitee, he falls due to the negligence of Block and breaks his arm. The next year the same customer returns to Block to have his taxes prepared and additionally to obtain an

RAL. He signs the RAL application with Household that contains the arbitration provision. He then files a court action to recover damages for the injuries he suffered when he fell and broke his arm. Because the personal injury occurred as a business invitee this could arguably involve the "relationship" between Block and the customer. Block would have it that this personal injury action, completely divorced from the loan application, would nonetheless be subject to arbitration. This is an absurd result. Clearly no reasonable consumer has contemplated, when applying for a loan, the application of an arbitration provision to a personal injury accident that occurred one year prior to the execution of the arbitration clause.

¶ 17 It is therefore clear that the existence of an arbitration provision and a liberal policy favoring arbitration does not require the rubber stamping of all disputes as subject to arbitration. Pennsylvania policy regarding arbitration is consistent with United States Supreme Court rulings. ***Lytle v. CitiFinancial Services, Inc.***, 810 A.2d 643, 653 (Pa. Super. 2002). The FAA merely placed arbitration agreements on equal footing with other contracts.[5] ***Id.***

¶ 18 In Pennsylvania the issue of whether a particular dispute falls within a contractual arbitration provision is a matter of law for a court decide. ***Huegel***, 796 A.2d at 354. To determine whether the claim is subject to arbitration the court engages in a two-prong analysis. First, does a valid agreement exist and second is the dispute within the scope of the agreement. ***Keystone Technical Group, Inc. v. Kerr Group, Inc.***, 824 A.2d 1223, 1227 (Pa. Super.

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[5] Prior to the enactment of the FAA in 1925, an arbitration clause was revocable at will by either party.

2003). The FAA specifically allows for the negation of an arbitration provision "upon grounds as exist at law or equity." Thus, generally accepted contract defenses such as duress, illegality, fraud or unconscionability are available to challenge the application of an arbitration provision. ***Lytle***, 810 A.2d at 656. In analyzing the contract, we must take care to note the surrounding circumstances, the situation of the parties when the contract was made, and the objects they apparently had in view and the nature of the subject matter. ***Huegel***, 796 A.2d at 354.

¶ 19 While any doubts about the intent of parties or enforceability of the arbitration provision should be resolved in favor of arbitration, the existence of a controversy regarding some aspect of an arbitration provision does not equate to "doubt." If that were so, then any dispute over the applicability of an arbitration provision would automatically be resolved in favor of arbitration leaving the court only to decide whether an arbitration provision had been executed. Given the recitation of the case law above, it is clear that the court's role is greater than simply determining whether a contract has been signed.

¶ 20 The trial court examined the circumstances surrounding the RAL application and the tax preparation. It considered the fees charged and the purpose for the fees. The trial court recognized that a person is fully able to obtain tax preparation services, including electronic filing, without ever applying for an RAL. Thus, the e-filing fee in question will be incurred independently of the application for the RAL. The trial court considered the fact that Block is not an actual party to the RAL, even though it is mentioned in the application document. We note that the RAL application specifically denies Block's status as fiduciary or agent in terms of the RAL.

¶ 21 In examining the circumstances of the contract in question, the arbitration clause appears in the loan application, not the tax preparation contract. The language of the arbitration clause refers to the "documents," documents being defined as the RAL application, not any contract or document prepared by Block. The provision refers to any controversy arising from the relationships of the parties. As noted earlier, this does not and cannot refer to all conceivable relationships between the parties; rather, viewing the document as a whole, the intent appears to be the relationships of the parties as it applies to the loan. This interpretation is further supported by the fact that Block has no direct connection to the RAL application. There is no signature required from any Block representative for the contract to be consummated. By all appearances, Block need not have actually even prepared the tax forms in question. At most, Block is a third-party beneficiary solely to the arbitration clause of a loan application. It simply makes no sense to provide Block with independent rights to enforce the arbitration provision of a contract it is not a party to, concerning an issue not covered by the contract. The "relationship" between Block, the customer and Household does not extend to Block, on its own, charging a customer a fee for putting an electronic postage stamp on a tax return.

¶ 22 Given all of the above, we cannot say that Judge Corbett in any way abused her discretion in finding that the electronic filing fee was separate and distinct from the loan application and therefore not covered by the arbitration provision.

¶ 23 The above discussion fairly well disposes of the notion that the two transactions, the RAL application and the e-filing fee are "intermeshed" to the point of inseparability. To

the above, we add a further comment. The argument made by Block ignores the reality that McNulty was charged an e-filing fee not only for the year she applied for a RAL, but for the prior year as well. Block offers no argument, nor can we perceive one, which would sufficiently explain how a fee charged one year before a loan request, regarding a transaction completely unconnected to the loan request, can in any way, shape or form be intermeshed with the loan request.

¶ 24 While we find no error in the trial court's ruling, we also note an alternative ground to affirm the denial of transfer to arbitration. Plaintiffs claimed that the arbitration clause was unconscionable and therefore unenforceable. The trial court noted its suspicions about the provision on unconscionability, but refrained from actually ruling on the issue. A complete review of the record, however, demonstrates that, as applied, this clause is unconscionable.

¶ 25 The FAA states that an arbitration provision may be challenged upon such grounds as exist at law or equity that may be used as a defense in any contract action. This allows for a challenge to the application of an arbitration provision based on such traditional grounds as duress, fraud, illegality and unconscionability. These issues are a matter of law properly determined by the courts.

¶ 26 A determination of unconscionability requires a two-fold determination: 1) that the contractual terms are unreasonably favorable to the drafter, and 2) that there is no meaningful choice on the part of the other party regarding the acceptance of the provisions. ***Lytle***, 810 A.2d at 658-59.

¶ 27 The contract in question is a classic example of an adhesion contract, which is a "form contract prepared by one party, to be signed by the other party in a weaker position, [usually] a consumer, who has little choice about the terms." ***Id.*** at 658. Thus, the second prong is met.[6]

¶ 28 Facially, the contractual terms do not appear to unreasonably favor either Block or Household. The provision does not reserve the right to trial solely to the drafter, a common reason for invalidating such a clause. Certainly, in many instances arbitrating a dispute involving a RAL would further the goals of saving all parties time and expense. However, as applied to the present factual scenario, it becomes apparent that the arbitration provision does unreasonably favor Block.

¶ 29 ***Lytle*** makes it clear that if the costs associated with arbitration of a single claim would operate to preclude a claimant from pursuing a remedy, then the enforcement of the provision would be unconscionable. ***Id.*** at 667-68. Here, the each single claim involves the imposition of a $34.00 to $37.00 fee. The arbitration clause states that the consumer is required to pay an initial $50.00 fee and then must pay any costs over the next $1,500.00. While we note that an arbitration hearing can often cost well in excess of $1,550.00, we have no evidence of how long an arbitration of each single case here would take and so have no clear picture of the ultimate cost of a single arbitration. Nonetheless, even

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[6] It must be noted that simply because a dispute involves an adhesion contract, that contract is not automatically unconscionable. ***Lytle*** at 658. However, the determination that an adhesion contract is at issue, by definition fulfills the second prong of the unconscionability test.

assuming no cost above the initial $50.00,[7] this arbitration clause requires a consumer to pay $50.00 in the hopes of receiving, at most $37.00. As Block points out in its brief, the IRS specifically allows for the imposition of some manner of fee for electronic filing,[8] therefore it appears unreasonable to presume the customer would be entitled to a refund of the entire fee. Thus, in reality the consumer would be spending $50.00 for a return of something around $30.00. While there may be a select few who are so incensed by the notion of the e-filing fee they would spend significant time and $50.00 for the possibility of a $30.00 award, this is a situation where the costs of arbitration, minimal though they may seem, work to preclude the individual presentation of claims.

> Avoiding the public court system to save time and money is a laudable societal goal. But, avoiding the public court system in a way that effectively denies citizens access to resolving everyday societal disputes is unconscionable. Goals favoring arbitration of civil disputes must not be used to work oppression. When the goals given in support of contract clauses like this are used as a sword to strike down access to justice instead of a shield against prohibitive costs, we must defer to the overriding principle of access to justice.

***Lytle***, 810 A.2d at 667-68 (***quoting Mendez v. Palm Harbor Homes, Inc.***, 45 P.2d 594 (Wash. App. 2002)).

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[7] This assumption necessarily presumes no cost for legal representation.

[8] IRS Publication 1345, handbook for Authorized IRS E-File Providers of Individual Income Tax Returns.

¶ 30 As applied to facts of this case, the enforcement of the arbitration provision would work to deny the allegedly injured parties access to justice and is therefore unconscionable.[9] We believe that this determination of unconscionability satisfies the FAA in that it represents grounds in both law and equity for the defeat of the arbitration provision.

¶ 31 For the foregoing reasons, order affirmed.

Judgment Entered.

/s/ [Illegible]
Prothonotary

Date: February 26, 2004

[9] We wish to reinforce the fact that the unconscionability of this arbitration provision is only in reference to the present factual situation.

## APPENDIX B

## IN THE SUPREME COURT OF PENNSYLVANIA
## MIDDLE DISTRICT

| | |
|---|---|
| ERIN M. MCNULTY AND BRIAN J. ERZAR, ON BEHALF OF THEMSELVES AND ALL OTHERS SIMILARLY SITUATED,<br>Respondents<br>v.<br>H&R BLOCK, INC., H&R BLOCK GROUP, INC., H&R BLOCK SERVICES, INC., H&R BLOCK TAX SERVICES, INC., H&R BLOCK EASTERN TAX SERVICES, INC., H&R BLOCK EASTERN TAX COMPANY, LLC; H&R BLOCK EASTERN ENTERPRISES, INC., AND H&R BLOCK EASTERN SUPPORT SERVICES, LLC.<br>Petitioners | : No. 241 MAL 2004<br>: Petition for Allowance of Appeal from the Order of the Superior Court |

### ORDER

**PER CURIAM**

**AND NOW**, this 1st day of July 2004, the Petition for Allowance of Appeal is hereby **DENIED**.

**TRUE & CORRECT COPY**
**ATTEST: JUL -1 2004**
/s/ Irene M. Bizzoso
**IRENE M. BIZZOSO, ESQUIRE**
**DEPUTY PROTHONOTARY**

## APPENDIX C

| | | |
|---|---|---|
| ERIN M. MCNULTY AND BRIAN J. ERZAR, on behalf of themselves and all others similarly situated, | : | IN THE COURT OF COMMON PLEAS OF LACKAWANNA COUNTY |
| Plaintiffs, | : | |
| v. | : | |
| H&R BLOCK, INC., et al | : | |
| Defendants | : | Docket No. 2002-CIV-4654 |

(Filed Apr. 16, 2003)

### MEMORANDUM AND ORDER

AND NOW, after consideration of the Defendants, H&R Bloc Inc., H&R Block Group, Inc., H&R Block Services, Inc., H&R Block Tax Service's, H&R Block Eastern Tax Services, Inc., H&R Block Eastern Tax Company, LLC, H&R Block Eastern Enterprises, Inc. and H&R Block Eastern Support Services, LLC's (hereinafter "Block") preliminary objections, the briefs, the supplemental memoranda and supplemental answers filed by all the parties, and oral argument, it is hereby Ordered and Decreed that the Preliminary Objections be overruled in part and sustained in part.

### I. BRIEF FACTS

Plaintiffs filed this class action lawsuit to recover on behalf of the Plaintiffs and other Pennsylvania consumers based on Block's practice of deceptively causing their tax return clients to pay millions of dollars in unnecessary tax return filing fees. Plaintiffs maintain that Block engaged in various illegal acts, including a company-wide practice

of collecting electronic filing fees by the deceptive method of portraying these fees as a necessary and required component of the standard tax preparation services provided by Block. This, Plaintiffs allege, allowed Block to collect exorbitant electronic filing fees even though it costs Block virtually nothing to perform the filing. All of this was allegedly unbeknownst to Plaintiffs.

On August 30, 2002, Plaintiffs filed a Complaint. On October 23, 2002, Defendants filed preliminary objections seeking dismissal of the Complaint. On November 4, 2002, Plaintiffs filed an Amended Complaint naming eight "H&R Block" entities as Defendants. On November 25, 2002, Block filed preliminary objections and on December 5, 2002, it filed its supporting brief. On December 13, 2002, Plaintiffs filed their response to Defendants' preliminary objections and their supporting memorandum was filed on December 26, 2002.

Thereafter, Plaintiffs filed an Amended Compliant. Defendants filed a Reply Memorandum in Support of its Preliminary Objections on January 21, 2003. Plaintiffs filed a Supplemental Answer to the Preliminary Objections on January 27, 2003. Oral argument, which was originally scheduled for December 11, 2002, was rescheduled. This matter is now ripe for decision.

## II. DISCUSSION

### A. FEDERAL ARBITRATION CLAIM

The Federal Arbitration Act ("FAA")[1] was enacted in 1925. *Lytle v. Citifinancial Services, Inc.*, 2002 PA Super

[1] 9 U.S.C. §§ 1-14.

327, 810 A.2d 643 (2002) It was a response to the common law doctrine "which provided that arbitration clauses were revocable at will by either party to the contract. *Id.* at 653. The FAA preempts any state statutes which tries to limit or restrict arbitration clauses or preclude their use in certain contract. *Id.* The FAA merely placed "arbitration agreements on equal footing with other contacts." *Lytle,* 2002 Pa. Super. at 653.

Pennsylvania's policy toward arbitration is consistent with the United States Supreme Court. *Id.* "The Pennsylvania Superior Court has stressed the deference afforded arbitration agreements by both federal and Pennsylvania courts, and concluded that 'Pennsylvania's policy toward arbitration is entirely consistent with the United States Supreme Court's holding.'" *Zoological Society of Philadelphia v. Intech Construction, Inc.,* 2000 WL 33252879, 48 Pa. D.&C. 4th 542 (2000).[2] "The [FAA] and the Pennsylvania Uniform Arbitration Act ["UAA"], and the case law that has developed under each, are functionally equivalent [with regard to] the authority of a district court to review an agreement to arbitrate and to stay or compel arbitration." *Id.* at 3.

When it comes to arbitration, the decisions of the Pennsylvania Courts have been governed by two propositions: "(1) arbitration agreements are to be strictly construed and . . . such agreements should not be extended by implication and (2) when the parties agree to arbitration in

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[2] Pennsylvania law regarding the enforceability of an agreement to "arbitrate is in accord with federal law and requires enforcement of arbitration provisions as written, permitting such provisions to be set aside only for generally recognized contract defenses such as duress, illegality, fraud, unconscionability." *Lytle,* 810 A.2d at 656.

clear and an unmistakable manner, then every reasonable effort will be made to favor such agreements." *Lytle,* 2002 Pa. Super. at 654. "Arbitration is a matter of contract." *Huegel v. Mifflin Construction Company, Inc.,* 2002 PA Super 94, 796 A.2d 350 (Pa. Super. 2002); *First Options of Chicago, Inc. v. Kaplan,* 514 U.S. 938, 115 S.Ct. 1920, 131 L.Ed.2d 985 (1995).

Arbitration is a method in which to resolve disputes, but only when all parties have specifically agreed to do so. *First Options,* 514 U.S. at 1924. It is for the court to determine if an agreement to arbitrate exists. *Huegel,* 796 A.2d at 354, citing *Smith v. Cumberland Group, Ltd.,* 455 Pa. Super. 276, 687 A.2d 1167, 1171 (1997). When making this determination, the court must first determine whether an express agreement to arbitrate was entered into between the parties. *Huegel,* 796 A.2d at 354, citing *Smith v. Cumberland Group, Ltd.,* 455 Pa. Super. 276, 687 A.2d 1167 (1997). In making that decision, state law governing the formation of contracts applies. *Lytle,* 810 A.2d at 643, citing *Webb v. Investacorp, Inc.,* 89 F.3d 252, 257 (5th Cir. 1996) (quoting *First Options of Chicago, Inc.,* supra); *Zoological Society,* 2000 WL 33252879.

In arbitration agreements, like any contract, it is the intentions of the parties which controls. *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth., Inc.,* 473 U.S. 614, 105 S.Ct. 3346, 87 L.Ed.2d 444 (1985). The "fundamental rule" in construing contracts, is to determine the intention of the parties and give effect to those intentions. *Huegel,* 796 A.2d at 354, citing *Lower Frederick Township v. Clemmer,* 518 Pa. 313, 543 A.2d 502, 510 (1988). It is the parties intentions, among other things, at the time the contract

was made that needs to be examined.[3] *Id.* Courts should adopt "an interpretation that gives paramount importance to the intent of the parties and ascribe the most reasonable, probable, and natural conduct of the parties . . . " *Zoological Society,* 2000 WL 33252879, citing *Midomo Co., Inc. v. Presbyterian Housing Development Co.,* 739 A.2d 180, 190-91. (Pa. Super. 1999). When it comes to issues of arbitration, the intent is to be "generously construed." *Mitsubishi Motors,* 473 U.S. at 626.

When analyzing a contract, all of its parts should be interpreted together. *Zoological Society,* 2000 WL 33252879. Each provision within the contract should be given effect. *Id.* at 3. This requires an examination of the entire contract (*Id.*), including taking into account "the surrounding circumstances, the situation of the parties when the contract was made and the objects [the parties] apparently had in view and the nature of the subject matter." *Huegel,* 796 A.2d at 354; *Odyssey Capital, L.P. v. Reddi,* 2002 WL 31663280 (2002). Parties should not assume that there is an agreement to arbitrate unless there is "clear and unmistakable" evidence that they did so. *First Options,* 514 U.S. at 1924.

Both federal and Pennsylvania law advocates "strict construction" of arbitration agreements and mandate that when doubts or ambiguities exist that doubt should be resolved in favor of arbitration. *Zoological Society,* 2000

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[3] "[I]t is well settled that in construing a contract the intention of the parties governs and that intention must be ascertained from the entire instrument taking into consideration the surrounding circumstances, the situation of the parties when the contract was made and the objects they apparently had in view and the nature of the subject matter." *In re Mather's Estate,* 410 Pa. 361, 189 A.2d 586, 589 (1963).

WL 33252879. Pennsylvania's courts favor the resolution of disputes by arbitration. *Huegel,* 796 A.2d at 354. While it seems obvious, it is important to note that if the parties did not contractually agree to arbitrate, they cannot be required to do so. *Lytle,* 2002 Pa. Super. at 653.

When a party is trying to prevent arbitration, the judicial inquiry is limited to determining: (1) "whether a valid arbitration agreement exists between the parties and, if so (2) whether the dispute involved is within the scope of the arbitration provision." *Zoological Society,* 2000 WL 33252879; *See also Paone v. Dean Witter Reynolds, Inc.,* 2001 Pa. Super. 350, 789 A.2d 221(2001) (reargument denied), citing *Flightways Corp. v. Keystone Helicopter Corp.,* 459 Pa. 660, 663, 331 A.2d 184, 185 (1975).

Defendants maintain that each of the Defendants applied for a Refund Anticipation Loan ("RAL") from Household Bank, f.s.b.[4] [5] According to the Defendants, the RAL applications each contained a binding arbitration provision governed by the Federal Arbitration Act, 9U.S.C. §1, et seq. While Defendants admit they are not parties to the RAL, transaction, they claim they are third party beneficiaries to the arbitration provision. Defendants maintain the arbitration provision contained in the RAL application applies.

Defendants claim the action must be pursued through arbitration and preliminarily objections to Plaintiffs proceeding with this action. (See PO's, pg. 5). Specifically, Defendants argue that the challenge to arbitration is

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[4] An RAL is a loan collateralized by the applicant's expected tax return.

[5] Household Bank, f.s.b. is not a named party in this action.

made in the wrong forum, and the arbitration provisions are valid and enforceable. Defendants insist that the Arbitration Provisions are enforceable because this case falls within the scope of the arbitration clauses of the RAL Agreements. They claim those provisions are not unconscionable or unenforceable and that the Agreements were not induced by fraud.

The Plaintiffs respond that the RAL Arbitration Provisions are inapplicable because this action arises out of Block's electronic filing services, not the RAL Agreement. Plaintiffs advance the argument that the electronic filing services are distinct from Block's financing facilitation services and the RAL relationship, and same are not applicable. Even if the RAL is so broad as to cover the electronic filing, Plaintiffs maintain that the arbitration provisions are unconscionable and unenforceable under Pennsylvania law, that they were facilitated by fraud and that, at a minimum, it is entitled to discovery relating to the arbitration provision.

### 1. Whether the Plaintiff's Challenge to the Arbitration Provision is in the Wrong Forum

Defendants first maintain that the Plaintiffs brought their challenge in the incorrect forum.[6] The applicable section in the Agreement states:

> I hereby agree that any claim, dispute or controversy, whether in contract, tort (intentional or otherwise, whether pre-existing, present or future, and including constitutional, statutory, common

[6] For McNulty, the Arbitration Provision is contained in ¶10 and in ¶11 for the Erzar.

> law, regulatory, and equitable claims with HB (as defined at the end of the paragraph) in any way relating to (a) the Documents or such similar documents for prior years, (b) advertisements, promotions, or oral or written statements related to RALs, and/or (c) the relationships of the parties, including the validity, enforceablity or scope of this Arbitration Provision or any part thereof (collectively the "Claim"), shall be resolved, upon the election of either me or HB by binding arbitration pursuant to this Arbitration Provision . . .

Defendants maintain this clause clearly shows that the Plaintiffs agreed to have an arbitrator and not a court decide the question of whether the parties agreed to arbitrate. As a result of this clause, Defendants argue that the claim should be forwarded to an arbitrator for determination.

As we have previously set forth, it is for the court to determine if an agreement to arbitrate exists. *Huegel,* 796 A.2d at 354, citing *Smith v. Cumberland Group, Ltd.,* 455 Pa. Super. 276, 687 A.2d 1167, 1171 (1997). Upon a finding that an agreement to arbitrate was entered into by the parties can it be forwarded to an arbitrator.[7] The case law cited shows this Court has the authority to determine whether the parties agreed to arbitrate. Defendants' preliminary objection to the contrary is overruled.

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[7] Importantly, if and when an agreement to arbitrate exists, depending upon the terms of that agreement, all issues related to the arbitration provision will then be forwarded to the arbitrator for decision. Thus, upon a finding that a valid arbitration agreement was entered into by the parties, issues such as its validity, enforceability, etc., would be decided by an arbitrator.

### 2. Whether a Valid and Enforceable Arbitration Agreement Exists

Defendants preliminarily object to the Complaint claiming that the claim falls within the scope of the Arbitration Provision and a valid arbitration agreement exists between the parties. In further support of that argument, Defendants maintain the Arbitration Provisions are not unconscionable, that the Arbitration Provisions were not induced by fraud and no discovery is needed prior to Arbitration.

At this point, it should be noted that Block provides tax preparation services to its customers. For a fee, it will file a customer's tax return electronically with the IRS. It appears that electronically filed tax returns enable taxpayers to receive their refund more quickly. For Block's customers who preferred not to wait that long, Block arranged for Household Bank, f.s.b. ("Household") to make a short-term loan in the amount of the anticipated tax refund. These loans are referred to as tax refund anticipation loans ("RAL").

Defendants' preliminarily object to Plaintiffs' Complaint arguing that the claims fall within the scope of the Arbitration Provisions of the RAL. They contend this matter needs to be decided by an arbitrator, not this Court. Defendants state that this "case most certainly involves the "relationship" between Block and Plaintiffs." Since the Plaintiffs entered into agreements which contained an arbitration provision, Defendants argue that those provisions "can be enforced in a proceeding concerning a different transaction between the same parties." (See

Def. Brief, pg. 3). Defendants cite *Huegel,* supra, as support for this argument.[8]

In *Huegel,* supra, homeowners brought an action against a contractor and a financing note holder for breach of contract, among other things. The defendants brought a motion to compel arbitration and the trial court dismissed the motion. The trial court ruled, among other things, that the "'third contract was signed separately and does not integrate either of the first two contracts' [the parties entered into] and therefore, 'the parties had agreed to arbitrate any disputes arising out of the problems surrounding the financing agreement, not the construction agreements.'" *Huegel,* 796 A.2d at 354.

The Superior Court ruled that the second and third contract "represent[ed] one transaction that culminated in the execution of the third contract. The court said the second contract contemplates the execution of a future agreement for financing." *Id.* at 355. It was "conditioned on the execution of the third contract." *Id.* at 356. Moreover, the court found that the third financing contract made "several references to the goods and services" that the Huegels were purchasing from the contractor which is further indication that this was one contract.

The Court has done an exhaustive examination of both the federal and state cases applicable to these proceedings. We have also made a detailed analysis of the contracts entered into between the parties. That being said, the contract in this case shows that the Arbitration Provisions apply to "the RAL Application and the Loan

[8] According to the Defendants, this is the same authority cited by Plaintiffs.

Agreement (Collectively the "Documents")." Arbitration applies for any claim specifically related to the "Documents" or such similar documents for prior years" It does not specifically or implicitly apply to the electronic filing service.

In fact, unlike Huegel, the "Documents" do not rely upon or even contemplate the electronic filing services being performed. If that were so, it would have to have some indication to same. Here, the "Documents" can exist whether the electronic filing services were even performed (i.e., mailed or otherwise forwarded to the IRS). It is also true that electronic filing can be done without entering into an RAL Agreement. One does not rely on the other.

For these reasons, we agree with Plaintiffs' contention that the electronic filing practices are separate and distinct from the RAL. They are not one transaction, but two separate and distinct transactions. Nothing in Defendants' preliminary objections or brief compellingly sets forth the contrary to be true. The mere mention of Block in the RAL docum without more, does not mean it applies to the narrow being made by the Plaintiffs. This is so since the elec nic filing can be done and often is done independently of the RAL. While the decision of this Court may have been different had the RAL and the electronic filing been intermeshed, the pleadings do not indicate this to be the case. For these reasons, Defendants' preliminary objections claiming the Arbitration Provisions apply is overruled.

Since we have held that the Arbitration Provisions in the RAL contract do not apply to the electronic filing claim brought by the Plaintiffs, it is not necessary for this Court

to address, nor could we, the other contentions regarding unconscionability, fraud or discovery.[9]

Still, in reviewing the terms of the RAL Agreements, the allocation of the costs related to the arbitration is troubling. The Arbitration Provisions apportion the fees as follows: On the claim [Plaintiff] file[s], Plaintiff will pay the first $50.00 of the filing fee. At [Plaintiff's] request, HB will pay the remainder of the filing fee and any administrative or hearing fees charged by the arbitration administrator, up to $1,500.00 on any Claim assented by me in the arbitration. If [Plaintiff] is required to pay any additional fees to the arbitration administrator, HB will consider a request by [Plaintiff] to pay all or part of the additional fees; however, HB will not be obligated to pay any additional fees unless the arbitrator grants me an award. If the arbitrator grants an award in [Plaintiff's] favor, HB will reimburse me for any fees paid or owed by [Plaintiff] to the arbitration administrator up to the amount of the fees that would have been charged if the original Claim had been for the amount of the actual award in my favor.

The contract does not specifically set forth what fees there will be. Although initially the Agreement does state that Plaintiff would have to pay Fifty Dollars ($50.00) and HB would have pay the next One Thousand Five Hundred Dollars ($1,500.00), the contract does not state what the total costs are related to the arbitration. This is troubling

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[9] If the Arbitration Provisions applied in this matter, it would appear that the claim of unconscionability and fraud would have to be addressed by the arbitrator according to the terms of the Agreement. These claims go directly to the terms of the RAL Agreements which contains the Arbitration Provisions.

because whatever the total costs are, it is HB's option of deciding whether it wants to pay any additional fees and costs. This makes Plaintiffs liable or potentially liable for a significant amount more than Fifty Dollars ($50.00). The potential fees may be cost prohibitive to a plaintiff bringing an action.

Moreover, according to the contract, even if the Plaintiff succeeds in arbitration, but receives something less than the full amount requested, the Plaintiff would have to pay any fees in excess of the One Thousand Five Hundred Dollars ($1,500.00).[10]

Again, although the information presented to this Court provides no evidence of the arbitration costs, the terms of the Agreement clearly provide that a plaintiff could be liable for significantly than more than what is specifically indicated. Many courts have held that arbitration fees which deter one from pursuing a claim are unconscionable. (See *Cole v. Bums International Security Servs.*, 105 F.3d 1465 (D.C. Cir. 1997) (An employee cannot be required to pay the arbitrator's fee to pursue his claim fees would discourage such action.); *Paladino v. Avnet Computer Techs., Inc.*, 134 F.3d 1054 (11th Cir. 1998) (Costs of $2000.00 filing fee and potential responsibility for the arbitrator's fee are costs which are a "legitimate basis for a conclusion that the clause does not enable people to vindicate their rights). Since we do not know the actual costs and have not had a hearing on same, the basis

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[10] This is how we interpret the language contained in the contract which states:

> ". . . if the original Claim had been for the amount of the actual award in my favor."

overruling the preliminary objection regarding arbitration is not based upon this observation.

* * *

An appropriate order follows.

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| | | |
|---|---|---|
| ERIN M. MCNULTY AND BRIAN J. ERZAR, on behalf of themselves and all others similarly situated, Plaintiffs, | : | IN THE COURT OF COMMON PLEAS OF LACKAWANNA COUNTY |
| v. | : | Docket No. 2002-CIV-4654 |
| H&R BLOCK, INC., et al Defendants | : | |

**ORDER**

(Filed Apr 11, 2003)

**AND NOW**, this 16th day of April 2003, upon consideration of the Defendants Preliminary Objections, the response, memoranda and supplemental responses and memoranda, it is hereby ORDERED and DECREED that:

1. Defendants' Preliminary Objection claiming that the Arbitration Provisions are applicable to the Plaintiffs' claims is OVERRULED;

2. Defendants' Preliminary Objection claiming lack of personal jurisdiction is OVERRULED without prejudice to Defendants revisiting this issue after discovery is done regarding jurisdiction;

3. Defendants' Preliminary Objections claiming legal insufficiency are OVERRULED in part and SUSTAINED in part;

a. The Preliminary Objection that the Plaintiffs' claims are preempted by federal law is OVERRULED;

b. The Preliminary Objection regarding alternative methods is OVERRULED;

c. The Preliminary Objections claiming the non-contract claims are barred by the Economic Loss and the "Gist of the Action" Doctrines are OVERRULED;

d. The Preliminary Objection to Plaintiffs' claiming no separate cause of action for breach of duty of good faith and fair dealing is SUSTAINED;

e. The remainder of Defendants' Preliminary Objections claiming no fiduciary relationship exists between the parties, no unjust enrichment was set forth and that nonfeasance cannot form basis of Unfair Trade Practices and Consumer Protection Law are all OVERRULED.

BY THE COURT:

/s/ Corbett, J.
TRISH CORBETT

## APPENDIX D

ARBITRATION PROVISION:

By signing this RAL application of the Loan Agreement (collectively the "Documents"), I hereby agree that any claim, dispute or controversy, whether in contract, tort (intentional or otherwise), whether pre-existing, present or future, and including constitutional, statutory, common law, regulatory, and equitable claims with HB (as defined below) in any way relating to (a) the Documents or a similar documents for prior years, (b) advertisements, promotions, or oral or written statements related to RAL, and/or (c) the relationships of the parties, including the validity, enforceability or scope of this Arbitration Provision or any part thereof (collectively the "Claim"), shall be resolved, upon the election of either me or HB, by binding arbitration pursuant to this Arbitration Provision and the applicable rules of either the American Arbitration Association ("AAA"), JAMS/Endispute ("JAMS") or the National Arbitration Forum ("NAF") in effect of the time the Claim is filed. The party initiating the arbitration proceeding shall have the right to select one of these three arbitration administrators. The arbitrator must be a lawyer with more than then (10) years of experience or a retired or former judge. In the event of a conflict between this Arbitration Provision and the rules of the arbitration administrator, this Arbitration Provision shall govern.

HB hereby agrees not to invoke its rights to arbitrate an individual Claim I may bring in small claims court or an equivalent court, if any, so long as the Claim is pending only in that court. No class actions or joinder or consolidation of claims with other persons, are permitted without the consent of the parties hereto. On any claim I file, I will pay the first $50.00 of the filing fee. At my request, HB

will pay the remainder of the filing fee and any administrative or hearing fees charged by the arbitration administrator, up to $1,500.00 on any Claim asserted by me in the arbitration. If I should be required to pay any additional fees to the arbitration administrator, HB will consider a request by me to pay all or part of the additional fees; however, HB shall not be obligated to pay any additional fees unless the arbitrator grants me an award. If the arbitrator grants an award in my favor, HB will reimburse me for any fees paid or owed by me to the arbitration administrator up to the amount of the fees that would have been charged if the original Claim had been for the amount of the actual award in my favor. If the arbitrator issues an award in HB's favor, I will not be required to reimburse HB for any fees HB has previously paid to the arbitration administrator or for which HB is responsible. Any participatory arbitration hearing that I attend will take place in the federal judicial district in which I live. This arbitration agreement is made pursuant to a transaction involving interstate commerce, and shall be governed by the Federal Arbitration Act, 9 U.S.C. Sections 1-16 (the "FAA"). The arbitrator shall apply substantive law consistent with the FAA and the arbitrator's award shall not be subject to appeal, except as permitted by the FAA. Upon request of either party, the arbitrator shall prepare a short reasoned written opinion supporting the arbitration award. Judgment upon the award may be entered in any court having jurisdiction. Nothing in this Arbitration Provision shall be construed to prevent HB's use of offset or other contractual rights involving payment of my income tax refund or other amount on deposit with HB to pay off any RAL debts or ERO or other fees now or hereafter owed by me to HB or any other RAL Lender or ERO or

third party pursuant to the Documents or similar prior documents.

I ACKNOWLEDGE THAT I HAVE A RIGHT TO LITIGATE CLAIMS IN COURT BEFORE A JUDGE OR JURY, BUT I PREFER TO RESOLVE ANY SUCH CLAIMS THROUGH ARBITRATION AND HEREBY KNOWINGLY AND VOLUNTARILY WAIVE MY RIGHTS TO LITIGATE SUCH CLAIMS IN COURT BEFORE A JUDGE OR A JURY, UPON ELECTION OF ARBITRATION BY HB OR BY ME. I ACKNOWLEDGE THAT I WILL NOT HAVE THE RIGHT TO PARTICIPATE AS A REPRESENTATIVE OR MEMBER OF ANY CLASS OF CLAIMANTS PERTAINING TO ANY CLAIM SUBJECT TO ARBITRATION, EVEN IF SUCH CLASS ACTION IS PENDING ON THE EFFECTIVE DATE OF THIS ARBITRATION PROVISION, EXCEPT THAT THIS ARBITRATION PROVISION WILL NOT PRECLUDE MY PARTICIPATION IN A CLASS WHICH HAS ALREADY BEEN CERTIFIED ON THE EFFECTIVE DATE OF THIS ARBITRATION PROVISION.

I understand that one or more affiliates of HB are defendants in several class action lawsuits challenging various aspects of HB's RAL program. Unless a class has been or is certified in one or more of these lawsuits prior to the effective date of this Arbitration Provision and the certification has not been overturned, I acknowledge that by signing the Documents, I may be giving up my right to participate as a member of such class if HB decides to arbitrate such a claim. This means I may not be able to obtain financial or other benefits which might ultimately be paid to or conferred upon members of the class.

This Arbitration Provision shall supersede any prior Arbitration Provision contained in any previous RAL application or loan agreement and shall survive repayment of my RAL and termination of my account. If any portion of this Arbitration Provision is deemed invalid or unenforceable, it will not invalidate the remaining portions of this Arbitration Provision.

As used in this Arbitration Provision, the term "HB" shall mean Household Bank, f.s.b., and H&R Block, Inc., and each of their parents, wholly or majority-owned subsidiaries, affiliates, predecessors, successors, and the franchisees of any of them, and each of their officers, directors, and employees.

Contacting Arbitration Administrators: If I have a question about the arbitration administrators mentioned in this Arbitration Provision or if I would like to obtain a copy of their arbitration rules, I can contact them as follows: American Arbitration Association, 335 Madison Avenue, New York, NY 10017, www.adr.org. Arbitration rules for the Resolution of Consumer-Related Disputes (applicable to requests for arbitration filed by a consumer involving a claim under $10,000), Commercial Arbitration Rules (for all other claims). JAMS, 45 Broadway, 28th floor, New York, NY 10017, www.jamsadr.com, Financial Services Arbitration Rules and Procedures, National Arbitration Forum, P.O. Box 50191, Minneapolis, MN 55405, www.arb-forum.com, Code of Procedure.